SCIMITAR
HYDROCARBONS
CORPORATION

1998 ANNUAL REPORT

CORPORATE PROFILE

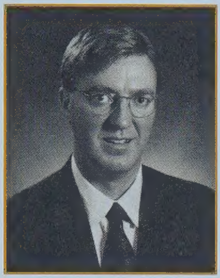
Scimitar Hydrocarbons Corporation is an international Canadian based petroleum company that commenced operations in late 1995 and trades on the Alberta Stock Exchange under the symbol SIY. Scimitar is connected to other successful companies through its key principals, the Mackenzie family, who have been responsible for founding and operating companies valued at more than C$1 Billion. Current projects include activity in Egypt, Ajman (United Arab Emirates), Canada, Kenya and Mozambique.

Scimitar's primary corporate focus is on international Discovered Reserve Opportunities (DROs). DROs are discovered producing properties and fields that for technical, fiscal or political reasons were not previously exploitable, but are now viable. Through its principals' extensive international network, Scimitar acquires large initial working interests in medium-size prospects with proven hydrocarbon potential.

Scimitar selects DROs with under-optimized, proven producing reserves, market access, and low development capital requirements and then employs proven, current, technical and business practices to capture the value inherent in those projects. Scimitar applies the lessons learned from acquisition and low-cost development strategies to capture value from higher yield projects in the international arena.

BOPD	Barrels of Oil Per Day
C$	Canadian Dollars
DROs	Discovered Reserve Opportunities
MMBBLS	Millions of Barrels
MMBO	Millions of Barrels of Oil
NPV10	Net Present Value Discounted at 10%
OOIP	Original Oil In Place
SPEL	Scimitar Production Egypt Limited
SPIL	Scimitar Production International Limited
TCF	Trillion Cubic Feet
US$	United States Dollars

MESSAGE FROM THE PRESIDENT



Jeffrey K. Brookman

This has been a year of dramatic change for Scimitar Hydrocarbons Corporation. In the spring of 1998, the company took action to reestablish its corporate focus within a turbulent and challenging global environment. The company's strategic mandate is now clearly focused. We are not a high-risk exploration company, nor are we a downstream marketing company. From this point forward the company will leverage off of our substantial international contact base to capture value from low-risk Discovered Reserve Opportunities (DROs). The company will create value from a variation of the proven successful, North American style property acquisition and low-cost development strategy.

The implementation of this strategic turnaround required a fundamental change to the company's operating philosophy. As a result, most of last year's Executive Management team and half the Board of Directors are no longer with the company. Angus Mackenzie, non-executive Chairman of the Board, provided stability through this period of transition.

During the last year we have experienced the effects of a climate influenced by turbulent financial markets, oil index declines, oil price drops and weakening currencies. Against this backdrop, Scimitar deviated from its strategic mandate, which is the exploitation of underdeveloped fields. The company, as it was then structured, invested the majority of C$15 Million from the January 1997 Special Warrant Issue into high-risk exploration in Mozambique. As with most high-risk ventures, the Mozambique drilling program met with limited success. These events, coupled with difficult market conditions, have resulted in the decline of Scimitar's share price to record low levels.

Scimitar has learned a lot during this difficult period. We have listened to our shareholders' concerns and are confident that our turnaround strategy will yield long-term, low-risk returns.

For fiscal 1999, the company is focused on developing cash flow from its Issaran (Egypt) oil development project. The exploitation business plan, under an independent assessment by Ryder Scott Company, places the proved reserve value of this project at US$42 Million using current pricing projections. Management is confident that this cost-focused plan for the development of Issaran will quickly realize dividends for our

shareholders. For the longer term, we believe that Issaran provides a stable platform from which to grow and capture additional DROs, both within Egypt, and in other regions of North Africa and the Middle East.

It should be stressed that the Issaran heavy oil project is not a typical heavy oil development. Issaran is characterized by high netbacks, moderate capital requirements and secured markets for the crude. This means that in soft market conditions, such as the recently experienced US$12 per barrel Brent crude oil price, the Issaran project can still generate positive cash flow. In addition, the development program has been designed to be extremely flexible so that the company can tailor its development program to suit market conditions and maximize cash flow.

Concurrent with our focus on DROs, the company is in the process of monetizing its non-core projects in Mozambique, Canada, Kenya and Ajman. This will be achieved through disposition, farmout or capitalization processes. Although these projects require little or no near-term capital, immediate monetization provides a funding vehicle for the pursuit and capture of future DRO initiatives. The company has successfully applied this concept to its joint venture project in Ajman.

I would like to thank our shareholders for their support and patience. We strongly believe our stock is undervalued in the current environment. Scimitar's current assets, coupled with the future value of our business development initiatives, provide a solid basis for significant appreciation in shareholder value. All of us at Scimitar – Board, Management and staff – are goal-aligned with you, the shareholders, to make investment in Scimitar a near-term success.

Jeffrey K. Brookman
Director, President, CFO and Secretary

STRATEGY

Recently, Scimitar's new Board of Directors and Management initiated an in-depth strategic review of the company's mission and its past performance. We recognized that Scimitar lacked the resources to create value through high-risk international exploration. In fact, the review told us that growth, for a company of our size, has to be achieved through other means. The DRO strategy is an ideal vehicle for sound fundamental growth. As a result, Scimitar is implementing a focused DRO strategy to capture value from under-optimized, proven producing reserves within the international arena. This low-risk technique is a variation of the acquisition and low-cost development strategy that has created value for a multitude of North American companies.

The plans we have implemented to facilitate this strategy include:

- Changes to the organizational structure.
- Changes to the operating philosophy.
- Creation of a cost focus culture.
- Focusing on financial considerations at a very early stage.

Within a clearly defined culture of cost consciousness, Scimitar's redefined Board of Directors and Management team are committed to success through the DRO strategy. Development of the Issaran oil field in Egypt is the top priority in Scimitar's low-risk DRO success strategy. Scimitar is aggressively working towards realization of production and cash flow from this core project.

To maintain a strategic focus on maximization of value through DROs, Scimitar is in the process of monetizing its entire exploration portfolio. This will be achieved through position dilutions, cross assignments and capitalization of new companies. An example of this monetization process is the company's recently negotiated carried working interest position in Ajman (closed on July 17, 1998). Variations of the monetization theme are being explored for Western Canada, Kenya and Mozambique.

REVIEW OF OPERATIONS

ISSARAN OIL DEVELOPMENT PROJECT, EGYPT

Major progress has been made on our core project, the development of the Issaran oil field in Egypt. This property, which has been operated since 1988 by the Egyptian state owned oil company, General Petroleum Company (GPC), is an underdeveloped, onshore oil field on the western side of the Gulf of Suez. The company negotiated breakthrough fiscal terms with the Egyptian government making incremental investment very attractive. On May 6, 1998, Scimitar signed a Petroleum Service Agreement (PSA) with GPC to develop the Issaran Oil Field Project. Scimitar's interest in the Issaran project is currently 100%.

The Issaran PSA is the first of its kind for the oil industry in Egypt and provides a win-win situation for both GPC and Scimitar. Under terms of the agreement, Scimitar fully funds the development program and in exchange retains a very high percentage of the incremental production volumes and associated revenue stream.

ISSARAN REVENUE SHARING TERMS

Production Level (BOPD)	Scimitar Interest before payout *	Scimitar Interest after payout *
3,000	85%	73%
10,000	80%	69%
20,000	75%	62%

* *After all taxes*

As shown, the percentages decrease with higher production levels and as payout is achieved. No other taxes or royalties are payable by Scimitar. These superior terms allow Scimitar to pursue the stage-wise assessment of the optimal recovery approach for Issaran with an excellent opportunity for a substantial return on investment. Through this innovative fiscal structure, Scimitar has overcome the typical heavy oil barrier-to-entry problem, the pricing differential from light to heavy oil. Issaran is competitive with light oil projects.

Recent Issaran developments include:

- Confirmation by Ryder Scott that the proved, primary, undeveloped reserve base of Issaran is 15.1 MMBO with an NPV10 of US$42 Million.
- Establishment of a strategic alliance with the GPC that provides Scimitar with a means to realize benefits from existing GPC service contracts, including rig contracts.
- Completion of the Purvin & Gertz crude price valuation report (confirming Scimitar's internal pricing estimates) and the establishment of price negotiations with the Egyptian General Petroleum Company (EGPC).

Scimitar believes that the potential exists to improve primary production levels from the current 750 BOPD to in excess of 10,000 BOPD through the application of horizontal drilling technology. In addition, the company plans to implement thermal recovery piloting technology developed in Western Canada, which could add further significant reserves.

Both Scimitar and its independent engineering consultants, Ryder Scott, estimate oil-in-place at Issaran to be in excess of 545 MMBO. The July 1 1998, Ryder Scott Reserve and Income Evaluation Report follows:

RESERVES ASSESSMENT (Ryder Scott, July 1998)

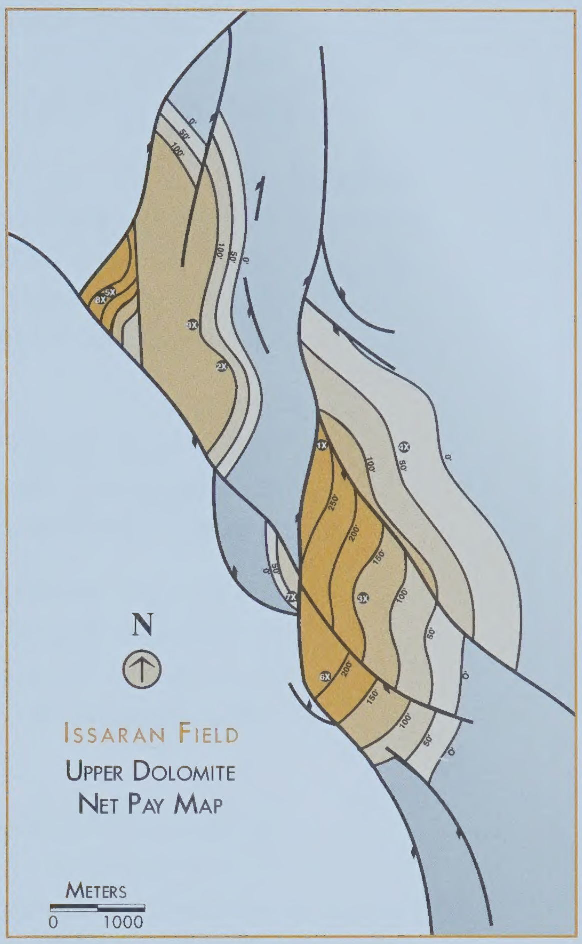
Gross Oil in Place (Million Barrels): 545					
Net Recoverable Company Reserves	(Million Barrels)	Net Present Value of Company Interest Escalating Pricing & Costs (US$Million)			
		0%	10%	12%	15%
Proved Undeveloped	15.1	60.2	42.3	39.5	35.6
Probable Undeveloped	6.0	6.8	4.0	3.6	3.0
Possible Undeveloped*	126.8	871.9	114.5	82.1	51.2
Total Proved, Probable and Possible	147.9	938.9	160.8	125.2	89.8

**Reflects reserve potential under thermal recovery*

As shown in the table above, Ryder Scott's study indicates that Scimitar's proved reserves at Issaran are in excess of 15 Million Barrels and are valued at over US$42 Million (at 10% discounting). In addition, over 100 Million Barrels of possible thermal reserves were recognized, with a possible NPV10 that is in excess of US$100 Million.

DESCRIPTION

The target reservoir zones are shallow, high porosity, dolomitic carbonates, which are areally extensive and characterized by thick pays with very good primary production capabilities. The development block has excellent access for new seismic and well drilling programs. Transportation infrastructure is well developed and underutilized. Markets exist for current and projected production.



DEVELOPMENT PLAN

Scimitar has applied current Western Canadian heavy oil technology to assist with the development of a sophisticated integrated reservoir model. The results from the initial phase of development will be used to refine and improve the reservoir model. This refined model will then form the basis for full field development. During the initial phase of development Scimitar intends to drill up to four horizontal wells, shoot a field wide 3D seismic program and initiate thermal recovery design studies.

Scimitar is in the final stages of negotiating the details of the financing arrangements for the Issaran development. Our projections are that field operations will commence in early 1999 with significant cash flow for the company in fiscal 1999.

MOZAMBIQUE

The second Mozambique exploratory well (Garabega #1) was dry and abandoned in November 1997. The target Grudja sands were porous but wet. We believe that world scale natural gas discoveries are possible in multiple objective horizons on the Buzi-Divinhe block. Arco's recent appraisal drilling at the Temane field, south of Scimitar's Buzi-Divinhe block, lends support to our assessment. World class reserves are being discovered within this geologic basin. Reserves at Temane have recently been expanded to 1.4 TCF.

The two wells drilled in Mozambique fulfill our work program obligations for the current and next exploration phase and earn Scimitar's 75% working interest in the Buzi-Divinhe block. Subsequent to drilling the two exploration wells, Scimitar elected to relinquish the Inhaminga Block, which is north of the Buzi-Divinhe Block.

The final phase of the work commitment (2000 - 2003) requires drilling two more wells prior to March 31, 2003. In the interim, Scimitar's monetization initiative for Mozambique can exploit a concept known as the "time value of land." This means that the company will be able to leverage off of the success of others within the region including Arco, Enron and BP.

Although we are confident that the intrinsic value of Mozambique will appreciate with time, the company has elected to take a write down of C$14,180,495. This reflects management's evaluation as to the future recoverability of exploration costs incurred to date.

AJMAN CONCESSION, UNITED ARAB EMIRATES

In the Ajman concession in the United Arab Emirates, Scimitar has reduced its working interest from 30 percent to a 10 percent carried working interest position. In exchange, the company received nearly US$200,000 and is carried on an onshore multi-well reentry program currently being drilled by the farmee.

CANADA

Scimitar completed a C$2.2 Million private placement of 2,762,500 special warrants on a flow-through basis in December 1997. These funds were used to cover expenditures related to Scimitar's 25% working interest in two Shell Canada operated exploration wells.

The wells were designed to test two large potential gas prospects situated in the deep basin region of Western Canada. The first well, drilled in Elmworth, Alberta, is plugged and suspended. The second well, drilled at Kelly in British Columbia is suspended. No further information may be released at this time for commercial competitive reasons.

KENYA

Scimitar and Trifoil Petroleum signed an agreement late in 1997 to market petroleum products in Kenya on a trial basis. The joint venture has been commercially unsuccessful to date, and the company will be divesting itself of its holdings in this endeavor. As a result, management has elected to write-down C$370,451 of the capitalized costs. This write down reflects management's evaluation as to the future recoverability of costs incurred to date.

OTHER PROJECTS

Scimitar is actively pursuing several international DROs that fit within our corporate strategic focus. The company recognizes that current soft market conditions provide an opportunity to capture additional assets under favorable terms. These new venture projects are in various stages of evaluation and negotiation.

INVESTOR INFORMATION

Scimitar received approval from the Alberta Stock Exchange to make a Normal Course Issuer Bid to purchase up to 1,154,955 (5%) of the outstanding common shares of the company on the open market. This bid remains in effect until February 23, 1999.

MANAGEMENT'S REPORT TO THE SHAREHOLDERS

The consolidated financial statements of Scimitar Hydrocarbons Corporation were prepared by Management in accordance with accounting principles generally accepted in Canada, and are consistent with the financial and operating information presented in this annual Report.

Management maintains a system of internal controls to provide reasonable assurance that all assets are safeguarded and to facilitate the preparation of relevant, reliable and timely financial information. Timely disclosure may require the use of estimates, in cases where transactions affecting the current reporting period cannot be finalized or known for certain until future periods. Such estimates are based on judgements made by Management, using all relevant information known at the time.

External auditors appointed by the shareholders have examined the consolidated financial statements and their report is presented below. The Audit Committee, consisting of a majority of non-management directors, has reviewed these consolidated financial statements with management and the auditors and has reported to the Board of Directors. The Board has approved the consolidated financial statements.

Jeffrey K. Brookman
Director, President, CFO and Secretary

AUDITORS' REPORT TO THE SHAREHOLDERS

We have audited the consolidated balance sheets of Scimitar Hydrocarbons Corporation as at June 30, 1998 and 1997 and the consolidated statements of net loss and deficit and changes in financial position for the years then ended. These financial statements are the responsibility of the corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the corporation as at June 30, 1998 and 1997 and the results of its net loss and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles.

KPMG. LLP.

Chartered Accountants
Calgary, Canada
September 23, 1998

CONSOLIDATED BALANCE SHEETS

June 30, 1998 and 1997
(Expressed in Canadian Dollars)

	1998	1997
ASSETS		
Current assets:		
Cash and short term deposits	$ 1,648,422	$ 13,987,030
Cash held in trust (note 4(d))	760,321	-
Accounts receivable	52,455	482,880
Prepaid expenses	12,624	4,988
	2,473,822	14,474,898
Capital assets (note 3)	7,207,439	8,445,106
	$ 9,681,261	$ 22,920,004
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued liabilities	$ 842,769	$ 857,715
Shareholders' equity:		
Share capital (note 4)	24,359,515	22,699,897
Deficit	(15,521,023)	(637,608)
	8,838,492	22,062,289
Future operations (note 1)		
	$ 9,681,261	$ 22,920,004

See accompanying notes to consolidated financial statements.

Approved by the Board:

Director

Director

CONSOLIDATED STATEMENTS OF NET LOSS AND DEFICIT

Years ended June 30, 1998 and 1997
(Expressed in Canadian Dollars)

	1998	1997
Pre-production revenues:		
Interest income	$ 559,072	$ 280,138
Foreign exchange gain	81,336	134,176
	640,408	414,314
Expenses:		
Write-down of petroleum and natural gas properties	14,550,946	-
Corporate general and administrative	877,137	640,948
Depreciation and amortization	95,740	96,229
	15,523,823	737,177
Net loss	(14,883,415)	(322,863)
Deficit, beginning of year	(637,608)	(314,745)
Deficit, end of year	$ (15,521,023)	$ (637,608)
Loss per share	$ 0.65	$ 0.02

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

Years ended June 30, 1998 and 1997
(Expressed in Canadian Dollars)

	1998	1997
Cash provided by (used in):		
Pre-production operations:		
Net loss	$ (14,883,415)	$ (322,863)
Write-down of petroleum and natural gas properties	14,550,946	-
Depreciation and amortization	95,740	96,229
	(236,729)	(226,634)
Investing:		
Additions to capital assets	(13,409,019)	(4,121,841)
Change in non-cash working capital	407,843	136,348
	(13,001,176)	(3,985,493)
Financing:		
Issuance of Common Shares and flow-through share purchase warrants, net of share issue costs	1,659,618	17,991,653
Increase (decrease) in cash and short-term deposits	(11,578,287)	13,779,526
Cash and short-term deposits, beginning of year	13,987,030	207,504
Cash, short-term deposits and cash held in trust, end of year	$ 2,408,743	$ 13,987,030

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Years ended June 30, 1998 and 1997
(Expressed in Canadian Dollars)

Incorporation:

Scimitar Production International Ltd. ("SPIL") was incorporated on March 15, 1995 in the British Virgin Islands. On November 10, 1995, SPIL was acquired by Commonwealth Energy Inc., a corporation incorporated under the Alberta Business Corporation Act. This acquisition was accounted for as a reverse take-over and the name of the combined companies was changed to Scimitar Hydrocarbons Corporation ("the Corporation") on January 2, 1996.

1. **Future operations:**

These consolidated financial statements are prepared in accordance with accounting principles generally accepted in Canada and have been prepared on the basis of accounting principles applicable to a going concern which contemplates the Corporation will continue to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future.

The Corporation's activities to date have been directed toward the acquisition of, exploration for and development of Canadian and international petroleum and natural gas reserves. The Corporation has acquired interests in undeveloped petroleum and natural gas interests in Canada, Mozambique, Egypt and United Arab Emirates. Production has not commenced in any location.

The ultimate recovery of the Corporation's investment in petroleum and natural gas properties is dependent upon the ability of the Corporation to have sufficient capital funding to successfully complete the exploration and development programs and find commercially viable hydrocarbon reserves which will ensure ongoing profitability.

Should the going concern basis of accounting be inappropriate, adjustments would be necessary to the recorded assets and liabilities and reported revenue and expenses.

2. **Significant accounting policies:**

(a) Basis of presentation:
These consolidated financial statements include the accounts of the Corporation and those of its wholly-owned subsidiaries and are expressed in Canadian dollars.

(b) Capital assets:
The Corporation follows the full cost method of accounting for petroleum and natural gas operations whereby all costs of exploring for and developing petroleum and natural gas properties and related reserves are capitalized into a cost centre for each country in which the Corporation has operations. Such costs include land acquisition costs, costs of drilling both productive and non-productive wells, geological and geophysical expenses and well equipment. Cost centres with capitalized costs for unproved properties are subject to ongoing management evaluation for impairment. In the event that it is determined that the unproved properties are impaired, the capitalized costs will be written down as a current direct charge to the statement of operations.

2. Significant accounting policies (continued):

(b) Capital assets (continued):

Upon commencement of production, capitalized costs will be depleted using the unit-of-production method based on estimated proven reserves of petroleum and natural gas before royalties. For purposes of the depletion calculation, natural gas reserves and production will be converted to equivalent volumes of crude petroleum based on the approximate relative energy content.

Gains or losses on the sale or disposition of petroleum and natural gas properties are not ordinarily recognized except under circumstances which result in a major revision of depletion rates.

The Corporation will annually apply a "cost recovery test" to capitalized costs to ensure that such costs do not exceed future net revenues from estimated production of proven reserves, using prices and costs in effect at the Corporation's year end. Future net revenues are calculated after deducting general and administrative costs, financing costs, income taxes and future site restoration and abandonment costs.

Depreciation of furniture and equipment is based on estimated useful life and is calculated using the declining balance method at rates of 20% to 40%.

(c) Joint interest operations:
Certain of the Corporation's exploration and production activities are conducted jointly with others and, accordingly, the consolidated financial statements reflect only the Corporation's proportionate interest in such activities.

(d) Future site restoration and abandonment costs:
Estimated future site restoration and abandonment costs, net of expected recoveries, will be provided over the life of the proved reserves using the unit-of-production method. Costs are estimated each year by management based on current regulations, costs, technology and industry standards. The annual charge will be included in depletion and actual removal and site restoration expenditures will be charged to the accumulated provision account as incurred.

(e) Flow-through shares:
The resource expenditure deductions for income tax purposes related to exploratory and development activities funded by flow-through share arrangements are renounced to investors in accordance with income tax legislation. Petroleum and natural gas properties and share capital are reduced by the estimated benefit of the renounced deductions when the expenditures are incurred.

(f) Foreign currency translation:
Monetary assets and liabilities are translated at the rates of exchange at the balance sheet dates. Non-monetary assets and liabilities are translated at the rates in effect at the dates the assets or liabilities were acquired. Revenues and expenses are translated at the average rates of exchange during the month in which they are recognized. The resulting gains or losses are included in earnings, except that foreign exchange gains or losses arising on translation of long-term monetary assets and liabilities are deferred and amortized over their remaining term.

2. **Significant accounting policies (continued):**

   (g) Measurement uncertainty:
   The amounts recorded for depletion, depreciation and amortization of capital assets and the provision for future site restoration and abandonment costs are based on estimates. The ceiling test is based on estimates of proved reserves, production rates, petroleum and natural gas prices, future costs and other relevant assumptions. By their nature, these estimates are subject to measurement uncertainty and the effect on the financial statements of changes in such estimates in future periods could be significant.

3. **Capital assets:**

	1998	1997
Undeveloped petroleum and natural gas properties:		
United Arab Emirates	$ 3,277,374	$ 3,453,466
Mozambique	100,000	3,753,342
Egypt	1,974,959	594,817
Canada	998,125	89,828
Other	761,716	469,232
Furniture and equipment, (net of accumulated depreciation of $68,397; 1997 - $40,753)	95,265	84,421
	$ 7,207,439	$ 8,445,106

During the year ended June 30, 1998, the Corporation $1,294,208 capitalized (1997 - $1,393,740) of international administrative and general corporate overhead costs related to the exploration for petroleum and natural gas properties. Of the total $1,294,208 capitalized, $177,329 (1997 - $228,197) related to head office general corporate overhead capitalized to specific projects in the current year. The remaining international capitalized administrative costs are identifiable with and charged to specific projects.

During the year ended June 30, 1998, the Corporation recorded a write-down of capitalized exploration, marketing and distribution costs in the amount of $14,550,946 (1997 - $nil). This write-down reflects management's evaluation as to the future recoverability of costs incurred to date on non-core upstream and downstream petroleum and natural gas assets in Mozambique and Kenya.

4. **Share capital:**

(a) Authorized:

Unlimited number of Common Shares

50,000,000 non-voting Preferred Shares

(b) Issued:

	Number of Shares	Amount
Common Shares		
Balance, June 30, 1996	12,674,310	$ 4,708,244
Issued on exercise of warrants	584,480	650,600
Issued on exercise of stock options	561,667	346,967
Issued through private placement for cash	3,547,322	3,015,224
Issued in exchange for Special Warrants	5,500,000	15,125,000
Issued in lieu of salary	78,236	70,000
Share issue costs	–	(1,216,138)
Balance, June 30, 1997	22,946,015	22,699,897
Issued on exercise of share purchase warrants	125,000	156,250
Issued on flow-through shares for cash	50,000	40,000
Issued in lieu of salary	120,543	185,313
Repurchased under normal course issuer bid	(286,000)	(133,634)
Share issue costs	–	(137,404)
Balance, June 30, 1998	22,955,558	22,810,422
Warrants		
Balance, June 30, 1997	–	–
Flow-through share warrants issued for cash	2,712,500	2,170,000
Deferred income tax impact of flow-through share expenditures	–	(620,907)
Balance, June 30, 1998	2,712,500	$ 24,359,515

(c) **Stock options:**

The Corporation has a stock option plan under which the Corporation has reserved 2,602,000 Common Shares for granting under option to directors, officers, employees and key consultants. The options become vested as to 33.3% annually following the date of grant.

At June 30, 1998, the Corporation had 2,602,000 (1997 – 1,672,333) stock options outstanding that are exercisable at prices ranging from $0.41 to $2.25 and expire on dates ranging from November 10, 2000 to May 19, 2003.

4. Share capital (continued):

(d) Warrants:

At June 30, 1998, the Corporation has 2,712,500 flow-through share purchase warrants outstanding, exchangeable for flow-through Common Shares of the Corporation on a one-for-one basis at no additional cost to the warrant holder. The flow-through share purchase warrants and proceeds received on the issuance of flow-through share purchase warrants are held in trust and released to the investor and the Corporation subsequent to the Corporation incurring qualifying expenditures in accordance with income tax legislation. The 6,397,222 share purchase warrants outstanding at June 30, 1997 were exercised or expired during the current fiscal period.

(e) Flow-through shares:

Pursuant to the flow-through share offerings, the Corporation renounced approximately $2,210,000 of qualifying expenditures effective December 31, 1997 of which approximately $2,210,000 will be incurred in calendar 1998.

(f) Loss per share:

The loss per share was calculated using the weighted average number of shares of 23,086,811 (1997 -18,365,078) outstanding during the period. A normal course issuer bid resulted in the weighted average number of shares being greater than the common shares outstanding at the end of the period.

5. Income taxes:

The provision for income taxes differs from the amount obtained by applying the combined Federal and Provincial income tax rates to income before income taxes. The difference relates to the following items:

	1998	1997
Loss before income taxes	$ (14,883,415)	$ (322,863)
Corporate tax rate	44.6%	44.6%
Expected income tax recovery	(6,638,003)	(144,000)
Unrecognized benefit of losses	6,638,003	144,000
	$ -	$ -

6. Financial instruments:

The Corporation's financial instruments recognized in the balance sheet consist of accounts receivable and accounts payable and accrued liabilities. The fair values of the financial instruments recognized in the balance sheet approximate their carrying amounts due to the short-term maturity of these instruments.

7. **Uncertainty due to the Year 2000 Issue:**

The Year 2000 Issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using year 2000 dates is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date. The effects of the Year 2000 Issue may be experienced before, on, or after January 1, 2000 and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant systems failure which could affect an entity's ability to conduct normal business operations. It is not possible to be certain that all aspects of the Year 2000 Issue affecting the entity, including those related to the efforts of customers, suppliers, or other third parties, will be fully resolved.

8. **Segmented information:**

In 1998, the Corporation continued the majority of its exploration activities in Canada, Egypt, Mozambique and the United Arab Emirates. The accounting policies are consistent for all segments.

June 30, 1998	United Arab Emirates	Mozambique	Egypt	Canada	Other	Total
Capital assets by cost centre	$ 3,277,374	$ 100,000	$ 1,974,959	$ 998,125	$ 761,716	$ 7,112,174
Corporate capital assets						95,265
Total capital assets						$ 7,207,439
June 30, 1997						
Capital assets by cost centre	$ 3,453,466	$ 3,753,342	$ 594,817	$ 89,828	$ 469,232	$ 8,360,685
Corporate capital assets						84,421
Total capital assets						$ 8,445,106

During the current fiscal year the Corporation incurred $1,054,466 (1997 - $869,145) in head office general corporate overhead, of which $177,329 (1997 - $228,197) was capitalized to various cost centres (note 3) and the remaining $877,137 (1997 - $640,948) was charged to pre-production operations.

9. **Comparative figures:**

Certain of the prior year's figures have been reclassified to conform with the current year's presentation.

CORPORATE INFORMATION

BOARD OF DIRECTORS

Angus Mackenzie	Chairman
Jeffrey K. Brookman	Director, President, CFO and Secretary
Gerald Mackenzie	Director
Robert S. Wynne	Director
Wasfi A. Ataya	Director
Theodor Hennig	Director
Charles E. Parnell	Director

MANAGEMENT & KEY STAFF

Mohamed M. Assem, B.Sc., M.Sc. - Acting General Manager, SPEL
Jeffrey K. Brookman, B.A.Sc., MBA - President and CFO
John L. Dragonetti - Director, Operations and President, SPIL
Philip Hawker - Acting Controller
Peter A. Lubey - Director, Exploitation Engineering
Niheriwa Maseliha - Assistant General Manager, Mozambique
Don H. Smith - Petroleum Engineering Advisor

SOLICITORS

Burnet, Duckworth & Palmer
Calgary, Alberta

BANKERS

Royal Bank of Canada
Calgary, Canada

Hong Kong Bank of Canada
Calgary, Canada

AUDITORS

KPMG LLP

REGISTRAR & TRANSFER AGENT

CIBC Mellon Trust Company

STOCK LISTING SIY

The Alberta Stock Exchange

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Designed and Produced by Equal Elements Inc.

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Printed in Canada